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Supreme Court of the United States

October Term, 1967

NORFOLK AND WESTERN RAILWAY COMPANY,
Appellant

v.

UNITED STATES OF AMERICA, et al.,
Appellees

On Appeal from the United States District Court
for the Southern District of New York

JURISDICTIONAL STATEMENT

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JURISDICTIONAL STATEMENT

Appellant Norfolk and Western Railway Company (N&W) appeals from the judgment of the United States District Court for the Southern District of New York, entered on October 19, 1967, dismissing appellant's complaint which sought to set aside an order of the Interstate Commerce Commission directing N&W, through a subsidiary, to acquire control of Erie-Lackawanna Railroad Company (EL), The Delaware and Hudson Railroad Corporation (D&H), and Boston and Maine Corporation (B&M), upon terms and conditions specified by the Commission, and submits this statement to show that the Supreme Court of the United States has jurisdiction of the appeal and that substantial questions are presented.

Opinion Below

The memorandum order of July 26, 1967, and the October 19, 1967, opinion of the statutory three-judge

court convened in the Southern District of New York are not yet reported, and copies are attached hereto as Appendices A and B. The report of the Interstate Commerce Commission, dated June 9, 1967, is reported at 330 I.C.C. 780 and the Commission's report on reconsideration dated August 10, 1967, as modified on September 1, 1967, is reported at 331 I.C.C. 22. Copies of the Commission's reports and orders have been lodged with the Clerk of the Court.

Jurisdiction

This suit was brought under Title 5, U.S.C. § 704 and Title 28, U.S.C. §§ 1336, 2284 and 2321-25 to annul and set aside the supplemental order of the Interstate Commerce Commission, dated June 9, 1967, in Finance Docket No. 21510, et al., as modified by its orders dated August 10, 1967, and September 1, 1967. The judgment of the district court dismissing this complaint was entered on October 19, 1967. Notice of appeal was filed in that court on October 31, 1967. The jurisdiction of the Supreme Court to review this order by direct appeal is conferred by Title 28, U.S.C. §§ 1253 and 2101(b).

Questions Presented

1. Did the district court err in failing to consider the impact of the Commission's erroneous projection of "normal" earnings on the Commission's ultimate conclusion that directing N&W to acquire EL, D&H and B&M as subsidiaries would preserve the viability of those three carriers and, accordingly, be consistent with the public interest?

2. Did the district court err in affirming the Commission's report and order although that order permits inclusion of fewer than all of the petitioners in the N&W system, even though the report contains no findings with respect to either the public interest in such partial inclusion or the proper terms therefor?

3. Did the district court violate the rule in *SEC* v. *Chenery Corp.*, 332 U.S. 194 (1947), in sustaining the Commission's conclusions as to petitioners' prospective "normal" earnings on the basis of evidentiary findings and conclusions neither considered nor adopted by the Commission?

4. Did the district court err in sustaining the Commission's findings as to "normal" earnings where such findings rested only on the Commission's assumptions and not upon evidence of record?

5. Did the district court err in sustaining the Commission's determination of the financial terms for inclusion despite the Commission's failure to rule upon exceptions directed to those terms?

6. Did the district court err in sustaining the Commission's departure from established administrative precedent in allocating consolidation benefits and fixing labor conditions where the Commission did not justify its action with rational findings?

7. Did the district court err in interpreting the mandate of this Court in *Baltimore & Ohio R. Co.* v. *United States*, 386 U.S. 372 (1967), to permit the Commission to refuse to consider alternatives to inclusion of EL, D&H and B&M in the N&W system, where the effect of such re-

fusal was to preclude determination of the ultimate fate of these carriers?

Statutes Involved

The statutes involved in this case are: Administrative Procedure Act, §§ 7(d), 8(b), 10(a), 10(c), 10(e), 5 U.S.C. §§ 556(e), 557(c), 702, 704, 706; Judicial Code, 28 U.S.C. §§ 1253, 1336, 1398(a), 2101(b), 2284, 2321-25; Interstate Commerce Act, § 5(2), 49 U.S.C. § 5(2). Also involved are Rules 19a and 82 of the Federal Rules of Civil Procedure. The text of these statutes and rules is attached hereto as Appendix C.

Statement

This is the so-called *Inclusion* case, the decision in which, according to this Court, would determine "the ultimate fate" of EL, D&H and B&M. *Baltimore & Ohio R. Co.* v. *United States*, 386 U.S. 372, 378 (1967). The Commission's order, however, does not accomplish this result. Moreover, even if the stockholders of one or two of the three carriers elect to sell to N&W pursuant to the terms of the order, the order fails to protect the public interest.

The proceedings before the Commission were initiated by EL, D&H and B&M filing petitions for inclusion in N&W. Such petitions were authorized by a condition (Appendix O) attached to the Commission's order approving N&W's merger with the Nickel Plate and related transactions. *Norfolk & W. Ry. Co. and New York, C. & St. L.R. Co. Merger*, 324 I.C.C. 1 (1964). Under Appendix O, the Commission retained jurisdiction to direct inclusion of the three carriers if "found consistent with the public interest . . . under such terms as may be

found equitable to all parties involved" (324 I.C.C. at 148). The right to judicial review of Commission action under Appendix O was expressly protected (324 I.C.C. at 148).[1]

After hearings on the petitions for inclusion, the Commission held that "mergers were nowhere in sight," because of the inequity of requiring N&W to assume the $464 million of long-term debt of the three railroads (330 I.C.C. at 801). The Commission did, however, order N&W to issue the equivalent of 1,335,763 shares of its common stock, having a current market value in excess of $130 million, to acquire the equity interest in EL, D&H and B&M through subsidiary corporations wholly owned by N&W. The Commission's conclusions that the prescribed financial terms were fair were based upon its projection of the "normal" earnings of the three petitioning railroads (330 I.C.C. at 799-800). The Commission's conclusion that inclusion of the three railroads "in N&W by way of control" would be in the public interest was also based upon the Commission's finding that the three railroads would have "normal" earnings sufficient to permit them "to continue providing adequate transportation service" as subsidiaries of N&W (330 I.C.C. at 795).

The so-called "normal" earnings found by the Commission far exceed the carriers' actual earnings,

[1] "If the foregoing condition, as more specifically set out in appendix O, is accepted by the applicants, it should be clearly understood that the Commission does not intend that such acceptance will foreclose or limit review of any decision which the Commission may make in disposing of a petition filed pursuant to the aforesaid condition of approval" (324 I.C.C. at 28).

even before any allowance is made for the impact of the Penn-Central merger upon their revenues:

	"Normal" Earnings as found by the Commission (Millions) (330 I.C.C. at 816, 819, 821)	Actual Earnings (Millions)			
		Ten-Year Average (1955-1964)	1965	1966	12 Months Ended Sept. 30, '67
EL[2]	$9.6	($9.4)	$0.0	$3.3	($8.6)
D&H	6.3	4.4	5.2	5.1	3.4
B&M	1.5	(2.0)	(0.6)	(1.5)	(1.7)[3]

( ) denotes loss

The great disparity between the actual earnings of EL, D&H and B&M and the "normal" earnings relied upon by the Commission, both in determining the public interest and in fixing the prices N&W has been ordered to pay for these three railroads, resulted from a series of adjustments made by the Commission to EL's 1965-1966 earnings, and to the 1965 earnings of B&M and D&H (330 I.C.C. at 813-814, 819, 821). The validity of the adjustments that the Commission made and its failure to make other adjustments, particularly in the light of these carriers' actual earnings in more recent periods, constituted the principal area of dispute in these proceedings.

[2]EL's earnings are shown after full contingent interest charges. Its reported earnings for 1965 and 1966 were $3.3 and $6.6 million, respectively (330 I.C.C. at 873), and its reported results for the first nine months of 1967 showed a deficit of $7.7 million. These reported earnings, however, are not comparable to the $9.6 million found by the Commission and do not show the earnings available to stockholders because they do not reflect $3.3 million of the $8.8 million of full contingent interest charges, which must be taken into account in determining EL's "normal" earnings (330 I.C.C. at 812, 816).

[3]12 months ended June 30, 1967.

The specific adjustments made by the Commission to produce its findings of "normal" earnings, as well as the Commission's general findings with respect to the public interest, presume that all three railroads will in fact be included in N&W "under conditions of four-way control" (*e.g.*, 330 I.C.C. at 792-794, 836). The Commission made no provision for the situation in which only EL, or only EL and D&H, would be included as a result of its order, although the inclusion of each of the three petitioning railroads is at the election of their respective stockholders.

On June 13, 1967, immediately following the service of the Commission's order, N&W filed a complaint in the District Court for the Western District of Virginia (No. 67-C-51-R), the only judicial district in which N&W had the right to bring the action under the venue statute (28 U.S.C. § 1398), asking that the order be set aside. On June 23, 1967, D&H filed a complaint in the Southern District of New York seeking judicial review of that part of the Commission's order which had prescribed the financial terms in such a way as to preclude D&H from obtaining tax benefits from the transaction. On July 26, 1967, the District Court for the Southern District of New York issued an order joining N&W as an involuntary plaintiff in the D&H action (App. A).[4] In

[4]There is not even a hint in the Committee Notes that the 1966 revision of Rule 19(a), upon which the district court relied to support its order, changed the concept of involuntary plaintiff so as to permit joinder of N&W in the D&H action. The holding of the district court that the concept was inadvertently expanded will come as a surprise to Professor Moore, who stated in 1967 (3 Moore, Federal Practice, p. 2101) that "The doctrine [of involuntary plaintiff] can properly be applied only where there is such a relationship that the absent party must allow use of his own name as plaintiff [as in patent owner-patent licensee situations]." *Id.* at Section 19.06, p. 2215.

its order dated August 10, 1967, the Commission satisfied D&H by altering the form of the transaction to produce the requested tax benefits (331 I.C.C. at 23-38), thus mooting D&H's action. The District Court for the Southern District of New York nevertheless required N&W to proceed as an involuntary plaintiff in the D&H action in that court, overruled N&W's objections to joinder and venue (App. B, pp. 4-8), and entered judgment dismissing N&W's complaint on the merits (App. B, p. 71).

The district court treated the complaint for judicial review as addressed solely to the financial terms of the order directing N&W to acquire the stock and control of the three railroads (App. B, p. 30), and brushed aside the public interest issues raised by the complaint. The district court refused to give separate consideration to N&W's complaint that specific steps in the Commission's determination of "normal" earnings lacked reasoned findings supported by substantial evidence, and based its refusal on the grounds that "logical perfection in every step" is not required (App. B, p. 49), and that "any overestimate of E-L's earning power was fully compensated" by "substantial tax benefits" which would accrue to N&W if EL failed to produce the "normal" earnings which the Commission had projected (App. B, p. 51).

Recognizing that the Commission's order, even if affirmed, would not result in the inclusion of B&M, and might not result in inclusion of D&H if its stockholders so elected, the district court struggled with the Commission's failure to make findings responsive to this situation. After undertaking to supply findings of fact

which the Commission itself did not make upon issues which it did not even consider, and after making a prediction that D&H stockholders would vote for inclusion, the district court sustained the Commission's order (App. B, pp. 56-61).

This appeal followed. In view of the recognized need for expedition in restructuring the Eastern railroad system (386 U.S. at 392), N&W does not raise before this Court the questions arising from the district court's unprecedented and erroneous holdings on its joinder as an involuntary plaintiff and venue. Instead, N&W asks that this Court review and set aside the Commission's unlawful order and remand the case to the Commission to provide a solution responsive to the realities of the situation.

The Questions Presented Are Substantial

This *Inclusion* case was regarded by both the Commission and the district court as the key needed to unlock the benefits of the Penn-Central merger without destroying three railroads now providing essential transportation service to the public. In its opinion last Term, this Court referred to the then-anticipated Commission order in the *Inclusion* case, stating (386 U.S. at 392):

> "If its order is attacked in court the hearing there can be expedited, as was this one, and an early determination made. We do not believe that this is too high a price to pay to make as certain as human ingenuity can devise, a just and reasonable disposition of this matter for all of the parties. After all, it is the largest railroad merger in our history and if not handled properly could seriously disrupt and irreparably injure the entire railroad system

> in the northeast section of the country—to the great detriment not only of the parties here but to the public convenience and necessity of the entire Nation."

It was thus recognized that questions directed to the propriety of the Commission's action in attempting a restructuring of the railroad system in the northeast present substantial issues of great public importance. And, quite apart from the magnitude and importance of the transactions themselves, the district court has committed errors of law which present substantial issues calling for plenary review by this Court.

1. *The Commission Has Not Found That Any Public Interest Would Be Served By Directing N&W To Acquire The Stock Of Deficit Railroads*

The district court based its decision on the false premise that "no substantial attack is made on the Commission's basic finding . . . that inclusion of E-L, D&H and B&M in the N&W system on proper terms is in the public interest" (App. B, p. 30). The district court thus treated all challenges to the Commission's findings of the "normal" earnings of those roads as related solely to the question of the price to be paid by N&W. This is not the premise on which the case was tried by the parties or decided by the Commission.

In deciding the public interest issue, the Commission concluded that the three railroads "if included in N&W by way of control, would be able to continue providing adequate transportation service," and the Commission based this conclusion on the explicit finding that "the normal earnings of each petitioner after inclusion will be sufficient to meet their fixed charges" (330 I.C.C. at 795).

The district court, disregarding the direct relationship between the Commission's findings of "normal" earnings and its conclusions with respect to the public interest issue, treated all questions concerning the Commission's findings of "normal" earnings as related solely to the fairness of the price N&W is required to pay. The district court thus dismissed all challenges to the several factors and adjustments that led the Commission to conclude that EL, D&H and B&M would each enjoy substantial "normal" earnings on the ground that the prescribed stock exchange ratios represented "informed judgment on all elements of value." Paramount among the elements considered, said the district court, were the tax benefits N&W would realize "even if E-L earned nothing," so that "any overestimate of E-L's earning power was fully compensated" by "substantial tax benefits" to N&W (App. B, p. 51). In short, N&W has been told that it has no grounds for complaint if, instead of the "normal" earnings forecast by the Commission, these railroads experience no earnings or accumulate deficits, because in such event N&W, through consolidated tax returns, can recoup the enforced purchase price from the United States Treasury in the form of deductions from N&W's own taxable income.

It is unfair to require N&W to risk an investment in the petitioning railroads on the premise that, even if they earn no income or sustain losses, N&W's investment will be protected by offsetting tax benefits. But even if it is assumed that N&W could recover its purchase price from the Treasury through reduced taxes, the public interest in maintaining rail competition in the areas served by EL, D&H and B&M will not be satisfied unless

these railroads have adequate earnings. The Commission has directed N&W to acquire these railroads as wholly owned subsidiaries. The primary reason for providing such inclusion, as is clear from the Commission's findings in the *Penn-Central* proceeding, is to preserve the transportation service which the three petitioners provide the public and which Penn-Central threatens to destroy. However, unless each railroad has sufficient earnings to make it a viable subsidiary of N&W in competition with Penn-Central, inclusion will not preserve its service for the public.[5]

The Commission and the district court simply refused to face the reality that EL, D&H and B&M are, collectively, a deficit operation even before the admittedly severe impact of Penn-Central on their revenues from competitive traffic.[6] Although the Commission based its order upon the assumption that as an independent railroad EL would have "normal" earnings of $6.2

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[5]There are prior examples of railroads going bankrupt despite stock ownership or control by major railroad systems. *E.g.*, Erie R. Co. Reorganization, 239 I.C.C. 653, 655 (1940); Central Railroad Company of New Jersey Reorganization, No. B 401-67 (N.D. N.J. March 1967).

[6]The Commission found that the three carriers would lose $16.34 million to Penn-Central as subsidiaries of N&W, offset by only $8.18 million of traffic gains (330 I.C.C. at 804, 806). The Commission found that the traffic losses need not be considered in determining the price that N&W must pay because of offsetting benefits to N&W in protecting N&W traffic, but that finding is beside the point in considering whether, after Penn-Central, EL, D&H and B&M will have sufficient earnings to meet their fixed charges and provide adequate transportation service.

Moreover, the Commission's finding is not supported by evidence. Such offsets were not even claimed by EL, whose own witness testified that "inclusion of EL as a subsidiary of N&W would not significantly offset that impact [of Penn-Central] on either road" (EL Stmt. 12, p. 42).

million,[7] EL actually lost $8.6 million for the most recent 12-month period, and at its present rate EL's loss for 1967 will apparently exceed $12 million. Moreover, these deficits were recorded by EL *after* receiving the full subsidy for commuter deficits from the State of New Jersey upon which the Commission relied in projecting "normal" earnings (see App. B, pp. 41-42). Similarly, the Commission's finding that B&M would have "normal" earnings of $0.4 million as an independent railroad (App. B, p. 52), is incredible in view of the fact that B&M has experienced deficits every year since 1957, including a deficit of $1.5 million in 1966 (330 I.C.C. at 879), and is operating at an even greater deficit in 1967.

The district court acknowledged "the decline in E-L earnings during 1967" (App. B, p. 39), but paid no further attention to the effect of this decline on EL's ability to provide necessary transportation service as a subsidiary of N&W facing Penn-Central competition. In marked contrast, the district court asserted that an attack upon the need for the Penn-Central merger itself "has been shattered by the results for the first half of 1967" (App. B, p. 9, n. 6), although the decline in the Penn and Central earnings was not so great as to convert the combined net income of Penn and Central into a deficit. The district court's treatment of 1967 results—taking them into account in upholding Penn-Central and disregarding them in upholding EL's inclusion—can only be explained by the district court's belief that N&W would be compensated

[7] $9.6 million "normal" earnings after full contingent charges (330 I.C.C. at 816), less operating savings ($1.8 million) and traffic gains ($1.6 million) found to result from N&W control of EL (330 I.C.C. at 813).

for "any overestimate of EL's earning power" by using the losses as tax deductions (App. B, p. 51).

There is no basis for the assumption that directing N&W to acquire stock control of three railroads which have, collectively, been operating at a deficit for the past decade, and which are currently operating at a deficit, will protect those carriers from the impact of Penn-Central and preserve their service to the public. The Commission has not faced the question of whether directing N&W to acquire deficit carriers is in the public interest, because the Commission found that each carrier would have substantial "normal" earnings. The district court avoided the critical question of the public interest by concluding that any overstatement of the "normal" earnings of these carriers was relevant only to the question of financial terms.

Because the district court treated the whole subject of EL, D&H and B&M earnings as relating merely to the fairness of terms and not at all to the public interest, there has been a complete failure to consider the ability of these railroads to obtain the earnings necessary for their survival as subsidiaries of N&W in competition with Penn-Central.

2. *There Are No Findings To Support Inclusion Of EL Alone, Or EL And D&H Without B&M.*

Assuming the validity of every feature of the Commission's order that N&W acquire the stock of EL, D&H *and* B&M, the order is still fatally defective in that it presumes inclusion of all three roads as a package whereas, in fact, at least one and possibly two components of that package will not be included under the order.

Every finding in the Commission's report, both with respect to the public interest in inclusion and the financial terms, assumes the inclusion of all three railroads as a package. For example, the traffic gains, as found by the Commission and used in computing "normal" earnings, explicitly assume "conditions of four-way control" (330 I.C.C. at 834, 836). Similarly, the calculation of losses of traffic to Penn-Central assumes that EL, D&H and B&M are all to be included as subsidiaries of N&W (330 I.C.C. at 806). And the Commission's whole discussion of the competitive situation of these three railroads emphasizes "their interdependence in providing a substantial part of [their] service" (330 I.C.C. at 793). The extent of this "interdependence" was clearly shown by the following findings (330 I.C.C. at 832):

> "EL's most important interchange point is Buffalo, where N&W is its most important connection. EL's third largest interchange is at Binghampton, N. Y. with D&H . . . .
>
> "D&H's largest interchange is with B&M at Mechanicville, N.Y. . . . D&H's second largest interchange is with EL at Binghampton, N.Y. . . . One of D&H's important transportation functions, therefore, is to serve as a link between EL and B&M.
>
> "B&M's most important interchange point is at Mechanicville with the D&H . . . ."

The public interest and the terms for inclusion of EL alone, or EL and D&H without B&M, depend upon the business that would be available to such combinations. And the traffic gains would necessarily be

less, and the losses to Penn-Central more, under either of these bobtailed combinations than under the four-way N&W-EL-D&H-B&M package which the Commission assumed. Without B&M, D&H would be a bridge line to nowhere, lacking enough traffic to justify its existence. And EL's viability would be severely curtailed if B&M or B&M and D&H were either no longer viable or allied with Penn-Central.

Thus, even if all of the Commission's findings were entirely correct under the premise upon which they were made, it is now apparent that the premise that all three railroads will be included under the Commission's order has no reality. B&M is not coming into the present N&W system on the prescribed terms; and whether D&H will come in on the prescribed terms is speculative.[8] And yet the Commission has made no findings as to what the "normal" earnings of EL and D&H would be as subsidiaries of N&W without B&M, or what the "normal" earnings of EL would be if it were included as a subsidiary of N&W without B&M and D&H. All of the Commission's findings about the "interdependence" of the three railroads indicate that the three railroads were consistently regarded as a package, and yet the Commission has directed N&W to include only a portion of that package, at the election of the stockholders of B&M and D&H.

The district court explicitly conceded that the Commission had made no findings whatever with respect to

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[8]As shown in the Jurisdictional Statement in the *Penn-Central* case, B&M is seeking the higher price that only the elimination of competition through affiliation with Penn-Central could justify and D&H's chief executive officer has indicated a similar purpose.

the ability of EL to survive if that carrier alone were to be included in the N&W system, but it refused to accept the normal consequences of that admission, stating (App. B, p. 61):

> "While the Commission made no finding as to E-L's Penn-Central losses in the event that D&H also were not included, rejection by D&H's stockholders is so unlikely, as we will later show, that we will not reverse on that ground."

Apart from the court's own investment analysis (App. B, pp. 66-67), the only "showing" made to support the district court's assumption that D&H stockholders will approve the prescribed terms was its reference to the representation of D&H counsel that the D&H Board of Directors had "unanimously resolved that D&H would recommend inclusion terms as fixed by the Commission" (Tr. 9/28/67, p. 150). However, D&H counsel was careful not to suggest that this meant that the stockholders would accept that recommendation, and he advised the court that the directors had decided not to submit the question to a stockholder vote at this time unless ordered to do so by the Commission (*id.* at 151-152). In view of the public statements of D&H's president, who represents its principal stockholder, any prediction that D&H stockholders will vote for inclusion is mere speculation.[9]

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[9]President Dumaine informed D&H's stockholders in a letter, dated August 21, 1967 (Bensel affidavit of 9/5/67, p. 8) that the Board would continue to explore "other alternatives that may be available to D&H" prior to presenting the matter to the stockholders. Mr. Dumaine subsequently made it plain that one of the alternatives he had in mind was that "D&H should become part of the merged Pennsy-Central" (Bensel affidavit of 9/5/67, pp. 8-9).

In short, although it recognized that the Commission had committed reversible error, the district court refused to reverse because of the court's own speculation that D&H stockholders would render the error harmless by voting to accept the terms prescribed by the Commission. But if the district court's guess is wrong and the D&H stockholders reject those terms, N&W will nevertheless be required to acquire EL as a subsidiary even though the Commission has never considered whether such inclusion, on the terms prescribed, is either in the public interest or equitable to N&W. Unless and until the D&H stockholders have actually voted to accept the prescribed terms, the Commission's failure to make findings with respect to inclusion of EL alone constitutes error which requires reversal.

The district court did recognize that B&M will not be included under the Commission's order (App. B, p. 67). But the court held that ". . . there is a sufficient finding . . . that B&M's non-inclusion would not undermine the fairness of the terms for the inclusion of E-L and D&H" (App. B, p. 61). The only Commission finding remotely related to the point, however, was the following passage in Commissioner Webb's report (330 I.C.C. at 840):

> "If B&M were not controlled by N&W but remained an independent carrier the net reduction in EL and D&H annual gross freight revenues would no doubt be greater. The record does not permit any reliable estimate of the increased loss. * * * Without B&M in the N&W system, it can also be properly assumed that the traffic losses of EL and

D&H to a Penn-Central system would be somewhat larger than estimated with B&M controlled by N&W. * * *" (Deletions by the Commission.)[10]

This finding certainly does not permit the conclusion which the court drew. Nor does the district court add anything by its effort to provide substance to the finding by speculating about B&M's "strongest reasons" for favoring a D&H interchange "If B&M is not included but remains independent" (App. B, p. 59).[11] The whole premise of the discussion is beside the point because B&M cannot remain independent. The Commission found in *Penn-Central*, and each of the homeless roads proved in this *Inclusion* case, that the consummation of the giant Penn-Central merger foreclosed their continued operation as independent carriers. That was what the decision

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[10]In the portion of the paragraph deleted by the Commission, Commissioner Webb had said that the additional loss "would not be so large as to alter the ultimate conclusion reached [with respect to the public interest]" (Webb Rep., p. 66). N&W took specific exception to that portion of Commissioner Webb's report as not supported by evidence (N&W Exceptions, p. 70, n. 39), and the Commission responded to N&W's exception by deleting that portion of the paragraph in adopting the finding as its own.

Under these circumstances the assertion of the district court that, although deleting the challenged statement, the Commission adopted it by implication (App. B, p. 59, n. 38) is manifestly incorrect, as is the court's reliance upon Pacific States Box & Basket Co. v. White, 296 U. S. 176, 186 (1935). That case upheld a state order against constitutional attack on the ground that the existence of supporting facts could be presumed and that the state statute required no findings of fact. The present case is governed by the Administrative Procedure Act which requires that federal agencies act upon evidence in the record and make findings with respect to each material issue (5 U. S. C. §§ 556(e), 557(c)).

[11]In the course of this discussion, the district court volunteered that D&H would be "possessed of trackage rights over PRR between Wilkes-Barre, Pa., and Hagerstown, Md." (App. B, p. 59). No such trackage rights have been authorized, and the Commission has found that there would be insufficient traffic to justify the operation of any trains over such a trackage right even if authorized (330 I.C.C. at 853).

last Term was all about. It was because the Commission had found that Penn-Central would destroy the three railroads as independent carriers that this Court directed delay in the consummation of Penn-Central until the permanent home of the three roads had been determined (386 U.S. at 375, 388, 390). Since the findings in *Penn-Central* establish that continued operation of the three railroads as independent carriers is precluded, it is wholly unresponsive to the problem to make findings on the premise that B&M "remains independent."[12]

The district court concedes that "the situation would, of course, be different if B&M were to become part of Penn-Central," but dismisses this possibility on its own finding that inclusion of B&M in Penn-Central might not be permitted or might somehow be conditioned to protect B&M's interchange with D&H "to the maximum feasible extent" (App. B, pp. 59-60). The inclusion of B&M in Penn-Central cannot be discounted by the court so long as the Commission has left the door open for B&M to negotiate for inclusion in Penn-Central and has refused, despite N&W's repeated requests, to foreclose B&M's inclusion in Penn-Central. No one has ever suggested what protection could be given in that event, or how it could be made effective.

B&M has made perfectly plain its purpose to ruin D&H and severely injure EL if "B&M were a

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[12]For the same reason, there is no reality to any of the "hypotheses" listed by the district court on the premise that D&H or B&M would remain "independent" (App. B, p. 58, n. 36).

member or ally of Penn-Central."[18] And the hard fact is that B&M is already an ally of Penn-Central, having realigned itself as a defendant in the *Penn-Central* litigation (App. B, p. 10). The impact upon EL and D&H of B&M's activity as an ally of Penn-Central will be felt immediately upon consummation of the Penn-Central merger since it is now perfectly apparent that, contrary to the premise upon which the Commission adopted the Appendix G conditions (330 I.C.C. at 355), B&M does not regard itself as a prospective "affiliate of N&W."

The Commission's order is therefore unlawful in failing to make findings responsive to the real issues which the case presented—the viability and price of EL alone, or EL and D&H without B&M. The district court erred in not setting aside the Commission's order on this ground.

3. *The District Court's Disposition Of The Issues Violates The Standards Governing Judicial Review Of Administrative Orders.*

As discussed above, the Commission's conclusion that the inclusion of EL, D&H and B&M in the N&W

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[18] "There is little point in putting D&H in any system without also including B&M therein. As the Commission observed, D&H's most important interchange is with B&M in Mechanicville. As N&W has stated, D&H would become a 'bridge line to nowhere' without B&M. As a neutral road, B&M has historically found it possible to work in close cooperation with New York Central on East-West traffic. If B&M were a member or ally of Penn-Central, B&M would obviously work together with that system for their joint benefit. EL, D&H and N&W would all suffer directly as the result of B&M's non-inclusion." B&M Brief, S.D.N.Y. 67 Civ. 2451, September 5, 1967, pp. 42-43.

system would be consistent with the public interest rested on its findings with respect to "normal" earnings. The district court, on the contrary, treated those findings as relevant only to the determination of the financial terms for inclusion. As a result, the district court disposed of the issues raised with respect to those findings on grounds which, whatever their merit in determining the fairness of the price N&W is required to pay, do not sustain the Commission's ultimate conclusion that inclusion is consistent with the public interest. The district court's affirmance of that ultimate conclusion thus rests on grounds not adopted by the Commission.

In dealing with the Commission's failure to make findings to support inclusion of EL alone, or EL and D&H without B&M, the district court compounded its error in refusing to set aside the Commission's order by attempting to justify its action on the basis of evidence which the Commission refused to consider.

Thus, the district court relied upon EL's evidence that "if E-L alone merged with N&W, its losses to Penn-Central would be $8.5 million" (App. B, p. 60). The Commission, however, found that "mergers were nowhere in sight" (330 I.C.C. at 801), and further found that "EL's losses as a subsidiary of N&W would be considerably higher" than $8.5 million (330 I.C.C. at 837). EL's own testimony in this record was that EL, as an independent railroad, would lose $44 million (Tr. 408), and EL's position was stated by its financial expert as follows (EL Stmt. 12, p. 42):

> "We have noted [EL's Traffic Vice President] . . . Schmidt's testimony covering the additional traffic

> which can be realized by N&W and EL as a result of their consolidation as well as the potential effect on EL and on N&W, as separate carriers, if the proposed Penn-Central merger should be approved. . . . *Witness Schmidt concludes that inclusion of EL as a subsidiary of N&W would not significantly offset that impact on either road.*" (Emphasis added.)

This was the record made by EL, the railroad with the data in its possession, and this record was accepted by N&W. The district court improperly undertook to reappraise this evidence, and criticized it on grounds not relied upon by the Commission in its report in this case (App. B, p. 60).

With respect to D&H, the district court went further and found (App. B, p. 61):

> "Even if that same figure [$1.3 million] be used [in determining the added losses to Penn-Central] for D&H as part of an N&W-E-L-D&H system, the impact [of Penn-Central] on net income would be offset by the $565,000 in control savings—itself a low estimate even if N&W does not merge with D&H as it apparently could—which were not credited to D&H on the cash option that N&W requested and will almost certainly exercise."

To reach this conclusion, the district court not only attempted to supply an administrative finding relating to D&H's Penn-Central losses as part of an N&W-EL-D&H system that the Commission itself did not make or even consider, but did so on grounds which the Commission rejected when it (1) found the amount of the control savings (330 I.C.C. at 819), (2) found that "mergers were nowhere in sight" (330 I.C.C. at 801) and (3)

found that D&H is *not* entitled to credit for operating savings in computing a cash price (330 I.C.C. at 818; 331 I.C.C. at 29, 30; see App. B, p. 36, n. 19). The district court thus disagreed with the Commission three times in one sentence in its effort to patch a fatal hole in the Commission's action. This effort of the district court to supply its own findings of fact on essential issues as to which the Commission failed to make findings is characteristic of its entire opinion.

Analysis of the district court's opinion reveals literally dozens of instances in which that court has undertaken to decide questions which are exclusively committed to the administrative agency, but as to which the Commission itself either made no findings at all or made findings inconsistent with the district court's findings and conclusions.

The district court's method of judicial review raises substantial issues for this Court, *first* because of the great public interest in these transactions, and *second* because the district court's whole approach to the case misconceived the proper function of a court in reviewing administrative action. The proper standard is set forth in *SEC* v. *Chenery Corp.*, 332 U.S. 194, 196 (1947):

> "[A] simple but fundamental rule of administrative law . . . is . . . that a reviewing court, in dealing with a determination or judgment which an administrative agency alone is authorized to make, must judge the propriety of such action solely by the grounds invoked by the agency. If those grounds are inadequate or improper, the court is powerless to affirm the administrative action. . . ."

The district court did not "judge the propriety of [the Commission's] action solely by the grounds invoked by the agency." Instead, the district court conjured up grounds that the Commission did not invoke to take the place of findings that the Commission either did not make at all or that were not supported by evidence.

The district court sought to justify its action by asserting that the *Chenery* rule was limited as follows (App. B, p. 69):

> "In *Massachusetts Trustees* v. *United States*, 377 U.S. 235, 248 (1964), the Court made plain that *SEC* v. *Chenery Corp.*, 318 U.S. 80 (1943), so heavily relied on by N&W, was intended only to establish the important point that a reviewing court could not affirm an agency on a principle the agency might not embrace . . . ."

This interpretation is wholly unsound. The *Massachusetts Trustees* case held only that *Chenery* was inapposite where the agency had merely failed to cite the pertinent section of a statute which admittedly authorized the action taken. *Massachusetts Trustees* did not authorize a reviewing court to supply findings not made by the Commission in an effort to sustain the Commission's order. Any such idea was dispelled by this Court's later decision in *Labor Board* v. *Metropolitan Life Ins. Co.*, 380 U.S. 438, 443-444 (1965):

> "For reviewing courts to substitute counsel's rationale or their discretion for that of the Board is incompatible with the orderly function of the process of judicial review. Such action would not vindicate, but would deprecate the administrative process for

> it would 'propel the court into the domain which Congress has set aside exclusively for the administrative agency.' *Securities & Exchange Comm'n* v. *Chenery Corp., supra*, at 196."

The opinion of the district court is a most extreme example of a reviewing court propelling itself into the administrative domain,[14] and the judgment below should be reversed on this ground alone.

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[14] The district court conceded as much in stating that "our discussion has revealed many ways by which, in our view, the Commission could support terms as favorable as it has established even if the Court should have held some of its subsidiary findings to be insufficient" (App. B, p. 69).

Conclusion

For the foregoing reasons, probable jurisdiction of this appeal should be noted and the case set down for full hearing on the merits.

Respectfully submitted,

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APPENDIX A

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

THE DELAWARE AND HUDSON RAILROAD CORPORATION, *Plaintiff*,	
BOSTON AND MAINE CORPORATION, *Intervening Plaintiff*,	
v.	67 CIV. 2451
UNITED STATES OF AMERICA, *Defendant*,	
INTERSTATE COMMERCE COMMISSION, *Intervening Defendant.*	

Memorandum on Motions to Set Schedule and to Join N&W.

The United States of America and the Interstate Commerce Commission have moved this Court to establish an expedited briefing schedule in this action; appended to their motion is a copy of the Amended Pre-Trial Order of the District Court for the Western District of Virginia in Norfolk and Western Railway Co. v. United States of America, Civil Action No. 67-C-51-R. We note the statement of the two judges signing this order that it appeared to them "that the issues raised in this action should be litigated in the United States District Court for the Southern District of New York," and the continuance of the Virginia action for a hearing by the full court including that issue on September 26, 1967. We note also that in directing the continuance the court

made clear that this "shall not be construed to prevent or delay consideration by the United States District Court for the Southern District of New York of all the issues raised in this action" and provided that "any party may file copies of the brief which it has filed on the same issues in the Southern District of New York in lieu of filing original briefs in this action."

In light of the evident belief of the two judges in the Western District of Virginia that we should go forward with this action and of the Supreme Court's mandate for expedited hearing and early determination, we think it is incumbent on us to set a schedule that will permit our deciding this action as soon as feasible. To that end it is

ORDERED that the parties observe the following schedule, which is identical with that established by the District Court for the Western District of Virginia:

(a) Plaintiff and intervening plaintiffs are directed to file any supplemental complaints on or before August 7, 1967, or 7 days following service of the order of the Commission on Petitions for Reconsideration, in Finance Docket No. 21510, *Norfolk and Western Railway Co. and New York Chicago and St. Louis Railroad Co.—Merger, etc.*, whichever date is later.

(b) Defendant and intervening defendants are directed to file their answers, together with such additional pleadings as may be deemed proper, on or before August 14, 1967, or 14 days following service of the order of the Commission on Petitions for Reconsideration, whichever date is later.

(c) Plaintiff and intervening plaintiffs may file responsive pleadings if they deem it advisable on or before August 21, 1967, or 21 days following service of the order of the Commission on Petitions for Reconsideration, whichever date is later.

(d) No additional motions or pleadings may be filed thereafter except by leave of court for good cause shown.

(e) Proposed exhibits, if any, must be filed with the Clerk of the court on or before August 21, 1967, or 21 days following the service of the order of the Commission on Petitions for Reconsideration, whichever date is later. Formal proof of exhibits will be waived unless objected to in writing on or before September 11, 1967, or 42 days following service of the order of the Commission on Petitions for Reconsideration, whichever is later.

(f) The brief of plaintiff and intervening plaintiffs should be filed on or before August 18, 1967, or 18 days following service of the order of the Commission on Petitions for Reconsideration, whichever date is later. The brief of defendant and intervening defendants should be filed on or before September 8, 1967, or 39 days following the service of the order of the Commission on Petitions for Reconsideration, whichever is later. Reply briefs, if any, should be filed on or before September 19, 1967, or 50 days following the service of the order of the Commission on Petitions for Reconsideration, whichever date is later. In the event the hearing is set at an earlier date, reply briefs should be filed on or before the hearing date.

The United States and the Commission have also moved for an order under F.R. Civ. P. 19(a) to join the Norfolk & Western as a plaintiff. We see no reason to doubt that such joinder comes within the words and the evident purpose of the greatly broadened provisions of the first sentence of amended Rule 19(a). We are not persuaded that the last sentence of the rule creates an obstacle; joinder of the N&W as an additional party plaintiff would not "render the venue of the action improper." Here venue rests on the act of the D&H in bringing this action and the defendants' waiver of venue objection; joinder of an additional plaintiff does not defeat venue under 28 U.S.C. § 1398.[1] The motion is therefore granted on condition that such joinder shall not prejudice any contention the N&W may wish to make in any court that the Western District of Virginia is the appropriate forum for review of the inclusion order. Since, in addition to challenging the inclusion order, the Norfolk & Western will doubtless oppose the claims made by the Delaware & Hudson and the Boston & Maine, it may file an additional brief on that issue on or before the date fixed for the filing of briefs by defendants.

The D&H and the B&M also occupy a dual position, as plaintiffs attacking the adequacy of the consideration afforded by the Commission and as defendants answering the N&W's position that the consideration is excessive. Accordingly they also may file an additional brief as defendants answering any such arguments. If Erie-

[1]The final sentence of the rule seems to have been framed in the light of the then venue provisions as to diversity actions, 28 U.S.C. § 1391(a).

Lackawanna should seek intervention as a defendant, its application will be granted and it may file a brief as such.

On the assumption that the Interstate Commerce Commission will rule on the petitions for reconsideration by mid-August, the action is tentatively set for final hearing, see F.R. Civ. P. 65(a)(2), on September 28, 1967, at 10 A.M.

HENRY J. FRIENDLY
U.S.C.J.

RICHARD H. LEVET
U.S.D.J.

EDWARD WEINFELD
Senior U.S.D.J.

July 26, 1967